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Achieving Cost Efficiencies in  
Commercial Activities

Statement of  
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Before the  
Subcommittee on Legislation and  
National Security  
Government Operations Committee  
House of Representatives



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ACHIEVING COST EFFICIENCIES IN  
COMMERCIAL ACTIVITIES

SUMMARY OF STATEMENT BY  
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OPERATIONS ISSUES

The Chairman of the Subcommittee on Legislation and National Security, House Committee on Government Operations, asked GAO to summarize key issues from its work on the Office of Management and Budget's A-76 program and to comment on how provisions of H.R. 4015, the "Commercial Activities Contracting Procedures Act of 1990," would address them. The A-76 program is designed to achieve efficiencies by encouraging competition between the federal workforce and the private sector for providing commercial services needed by government agencies.

GAO believes that the A-76 program's concept of encouraging competition is a sensible management approach that can contribute to more efficient and effective government operations. However, despite its conceptual appeal, the program has not gained governmentwide acceptance or met its objectives.

Several key obstacles have hindered implementation of the A-76 program. The cost-study process is burdensome and time-consuming. The absence of workload data and adequate cost accounting systems has increased the time it takes to do studies and in some cases has contributed to increased contract costs. The A-76 program adversely affects federal workers' morale and reduces individual and organizational productivity. The accuracy of savings estimates and the extent to which savings are realized is open to question. The lack of convincing savings data has contributed to increasing congressional concern about whether program savings exceed its costs in disruption, diversion of energy, and program and contract administration.

Legislating a commercial activities cost-study program, as proposed in H.R. 4015, would remove any doubt about the program's priority and should increase the level of governmentwide cost-study activity. GAO believes that providing the program with a legislative foundation would result in agencies assigning a higher level of priority and resources to doing cost studies. Also, in theory, requirements for agencies to collect and report activity cost and savings data should result in more accurate cost studies and more reliable savings estimates.

However, GAO believes that legislation by itself may not completely dispel several key problem areas that have historically hindered A-76 implementation. GAO points out several such problems for the Subcommittee's consideration.

Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to discuss our work involving the Office of Management and Budget's (OMB) Circular A-76 as the Committee considers H.R. 4015, the "Commercial Activities Contracting Procedures Act of 1990." We have done considerable work on A-76 issues, most of which pertains to the Department of Defense (DOD), which has been the most active agency in implementing A-76.

The objective of the A-76 program is to achieve efficiencies by encouraging competition between the federal workforce and the private sector for providing quality commercial services needed by government agencies. H.R. 4015 would provide a legislative basis for this long-standing policy.

We believe the A-76 program's concept of encouraging competition is a sensible management approach that can contribute to more efficient and effective government operations. However, despite its appeal on a conceptual level, the program has failed to gain governmentwide acceptance or to meet its objectives.

We have found that DOD managers generally agree with the A-76 concept of government-private sector competition and accept its objectives of seeking efficiencies and cost savings. However, managers also say that the program is time-consuming, difficult to implement, disruptive, and threatening both to them and their employees. Our work has also shown that some agencies were confused about whether the A-76 program was strictly a contracting-out program or a program to gain efficiencies through competition.

Congress also has not fully accepted the A-76 program and has excluded certain activities or locations and imposed other restrictions over the years. Congressional concern about the

program has been exacerbated by the lack of convincing data that real savings from the program exceed its costs in disruption, diversion of energy, and program and contract administration.

#### LEGISLATING AN A-76-TYPE PROGRAM

At the same time that congressional restrictions and limitations on A-76 have been increasing, OMB has been sending an entirely different message to agencies. In November 1987, Executive Order 12615 was issued, which among other things, significantly increased agency annual position study targets and mandated that agency budgets be reduced at the beginning of each fiscal year to reflect estimated savings from planned A-76 studies. We believe that the conflicting signals from Congress and the Executive Branch have created confusion and has put agencies in a difficult situation.

As we have said in the past, legislating a program to gain efficiencies in commercial activities would remove doubt about the priority and status of the program. A legislated program, as defined in H.R. 4015, would also dispel ambiguity about such a program's intent, which is to achieve efficiencies in the government's commercial activities by encouraging competition between the federal workforce and the private sector. In theory, providing a legislative basis for a commercial activities cost-study program should result in an increased number of cost studies and more consistent governmentwide implementation. Because agencies would be required by law to make inventories of commercial activities publicly available and conduct cost comparison studies, agency heads would likely assign a higher level of resources and priority to doing A-76 work than they have in past years when they routinely failed to meet study goals.

However, on the basis of our experience, I want to point out several key problem areas that have historically hindered A-76

implementation that legislation by itself may not completely dispel.

BURDENSOME, TIME-CONSUMING  
COST STUDY PROCESS

We have reported that carrying out A-76 studies is a burdensome and time-consuming process. For example, we have found that on average, it took DOD about 2 years to complete individual cost studies, with some studies taking 8 years. Recent information from DOD shows that studies may be taking even longer to complete. As of January 1989, there were 940 cost studies underway. Of these, 411, or 44 percent of the studies, were started in fiscal year 1983 or earlier, representing 6 or more years in process. We see several factors contributing to the time taken to complete cost studies.

First, we have found that in most agencies, preparation of the performance work statement (PWS), which defines the government's requirements, is done as a collateral duty by employees in the function being studied. In addition to its being extra work, preparation of a PWS involves tasks these employees are often not skilled in and may never do again. For the most part, these employees lack the analytical expertise needed to precisely define the standards of performance and quantity of current and future workloads. We believe that the frequent lack of staff with the requisite professional skills to lead cost studies has contributed to the length of time it takes to do them.

Second, the absence of workload data and adequate cost accounting systems has in some instances extended study times and contributed to poorly prepared PWSs, which ultimately resulted in increased contract costs. When such systems are lacking, the A-76 cost-study process is lengthened, and those doing the study must do much more work to determine what the activity being

studied actually accomplishes. For example, a 1984 study by the Army Inspector General identified the absence of management information systems to collect accurate workload data as a problem in PWS preparation. Past GAO audits have shown that tasks omitted from the PWS were later added to the contract, resulting in increased costs. Contract cost increases have contributed to a growing congressional concern that the A-76 program does not produce savings.

Third, we believe that some agencies do not place a sufficiently high priority on making sure cost studies move quickly through the various points of review, especially if those reviewers are outside the A-76 office or the studied function. For example, a study might stay with an attorney or a personnelist for some time, while their attention is given to higher priority work of their offices.

Legislating an A-76-type program may help solve some of these problems. As I mentioned earlier, one possible benefit of a legislatively based program would be the assignment of a higher priority to the program by agencies. Perhaps one by-product of a higher priority would be greater focus by agency management on the level of resources needed to produce accurate and timely studies. This change could result in the establishment of a cadre of experts to lead the cost-study process. Such a cadre, thoroughly familiar with management-engineering techniques and other management analysis methodologies, could supervise the drafting of a PWS in concert with employees from the studied function. We believe that this approach could result in more accurate PWSs and reduce the burden and time of doing cost studies.

H.R. 4015 includes a provision for calculating all relevant costs of doing a commercial activity. We agree and believe that workload data should be kept on commercial activities. We have

reported that staff involved in doing cost studies have experienced difficulty in precisely defining the standards of performance and quantity of workload that the government is providing and expects to provide. The absence of workload data can lead to incomplete and ambiguous PWSs, which in turn can result in increased costs if the function is contracted out. We feel that agencies should begin collecting workload data for a function to be studied at least as soon as that study is announced. We believe that the requirements contained in H.R. 4015 should result in agencies' having more factual information, rather than guessing at workload data.

#### A-76'S ADVERSE EFFECTS ON EMPLOYEE MORALE AND PRODUCTIVITY

Because employees affected by an A-76 study face uncertain employment futures, the A-76 program adversely affects federal workers' morale and productivity. Our work has shown that employee anxiety can begin as soon as an A-76 study is announced. Some affected employees begin to look for new jobs, reducing individual and organizational productivity and frequently resulting in the loss of good employees. As attrition rates increase, managers frequently are required to accomplish essential functions with fewer workers. The lengthy cost-study process further compounds the problems for employees and management alike.

In a 1985 report on the program's impact in DOD, we found that the majority of federal workers whose jobs had been contracted out obtained other federal employment. We said that of 2,535 DOD employees we sampled who were in functions contracted out in fiscal year 1983, 74 percent had found other government jobs, most often at the same installation; 7 percent went to work for the contractor; 5 percent were involuntarily separated; and most of the remaining 14 percent resigned or retired. Of those who

obtained other government positions, about 56 percent received lower grades, and about 44 percent received the same or higher grades. A follow-up study of the 5 percent who were involuntarily separated showed that over half were eventually reemployed with the federal government, most at the same grade or lower.

A senior DOD official has said that one of the problems with A-76 is that "good employees leave, while others worry about keeping their jobs and do not do their jobs." He observed that the private sector does not intimidate employees with possible loss of employment if they do a good job. The program's effect on morale and productivity is one of the areas that must be addressed if the program is to have wider implementation.

H.R. 4015 would, perhaps for the first time, emphasize the various programs designed to help employees displaced by cost studies find jobs. It would also provide for placement assistance in the private sector. These provisions could give employees some degree of relief from the specter of losing their jobs as the result of a cost study.

H.R. 4015 also expands employee opportunities to participate in the cost-study program by allowing them to review, comment on, and recommend changes to PWSs and provides an opportunity to challenge cost study decisions. While we believe that these provisions could generally reduce employee anxiety about the cost-study process, employees whose jobs are directly threatened would still be understandably concerned about their future.

While these provisions may contribute to some improvement in employee morale and acceptance of the program, we believe that the provisions would also increase the time required to do cost studies. For example, H.R. 4015 provides affected employees with a new appeal right. Employees would be given at least 60 days in



which to comment on PWSs and recommend changes. If employees were not satisfied with their agencies' responses, they would have an additional 30 days to appeal to the agency review board. In addition, under H.R. 4015, employees would have 30 days to appeal the adequacy of a cost comparison analysis. This provision is similar to current A-76 policy, in which a 15- to 30-day period is provided for appealing cost-comparison determinations. However, one area of uncertainty under H.R. 4015 is the length of time that appellate bodies would have to adjudicate appeals. Current OMB policy provides for agencies to decide employees' appeals within 30 days of receiving them. H.R. 4015 does not set time limitations for these reviews. Taken together, these appeal periods could lengthen the cost-study process.

ADDITIONAL POINTS TO  
BE CONSIDERED

On the basis of our work in the area, we have eight additional points we would like to raise with you as you consider this legislation. First, H.R. 4015 does not contain standards for judging agency performance and holding agencies accountable for their activities. Neither does it contain enforcement provisions. Thus, it will be difficult to determine whether the bill's intent has been realized and to take corrective action, if needed.

Second, H.R. 4015 would emphasize the importance of collecting and reporting information on cost-study activities. We believe that reporting data on cost-study activities is a sound idea. To comply with these requirements, agencies will need accurate and complete information on A-76 program activities. For example, H.R. 4015 calls for savings to be reported annually to Congress. We recently reported that DOD's reported A-76 savings are neither

complete nor accurate.<sup>1</sup> We said that as a result, OMB's figures do not accurately reflect the extent to which economy in government operations is being achieved. Reliable information does not exist with which to assess the soundness of savings estimates, and neither OMB nor DOD knows the extent to which expected savings are realized. We recommended changes that would provide better data on A-76 savings.

We believe that collecting complete and accurate A-76 data is a significant issue because sound data would answer the fundamental A-76 question--does the program ultimately save money? As I said earlier, the current absence of good data is part of the reason for congressional, managerial, and employee skepticism about the program.

Third, the bill also would require agencies to periodically survey their commercial activities in an effort to use the most economical method of providing the service. Currently, once a commercial activity has been contracted out, agencies rarely consider whether it is more economical to bring it back in-house. Thus, little is known about the expense that may be involved in bringing a function back in-house once it has been contracted. Finding employees to do the work and procuring necessary equipment may be difficult and costly.

Fourth, legislating an A-76 type program gives it a status and emphasis that could affect agencies' participation in other efficiency-related programs. For example, besides A-76, other OMB programs--the Productivity Improvement Program and the Privatization program--also are aimed at gaining efficiencies. We recommended in our May 1989 report that agency managers should be allowed to choose which mix of these programs they want to use

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<sup>1</sup> OMB Circular A-76: DOD's Reported Savings Figures Are Incomplete and Inaccurate (GAO/GGD-90-58, Mar. 15, 1990).

to achieve efficiency goals.

In our May 1989 report, we also recommended that responsibility for A-76 be moved from the Office of Federal Procurement Policy (OFPP) and combined with other OMB programs designed to achieve operational efficiencies. We made this recommendation because we believed that managing A-76 from OFPP gave the appearance that A-76 was exclusively a contracting-out program. OMB has recently implemented this recommendation, and it is too early to show material benefits from this reorganization. H.R. 4015 would place responsibility for A-76 back with OFPP. We do not think this organizational placement worked well in the past and recommend that the Committee reconsider this provision.

Fifth, H.R. 4015 provides that the entire term of a contract for commercial activities should not exceed 3 years. As I mentioned earlier, it took DOD an average of about 2 years to complete individual cost studies, with some studies taking up to 8 years. Under the provisions of H.R. 4015, and assuming a 2-year average time frame for cost studies, a new cost study would have to start by the beginning of the second contract year in order to decide whether the activity would remain under contract or would be brought back in-house. Under these conditions, agencies could find themselves in almost a perpetual cost-study cycle for the same commercial activity. Until a less burdensome and time-consuming study process is developed, the 3-year limit may be too stringent.

Sixth, the definition of inherently governmental functions is a critical threshold issue that determines what activities can and cannot be considered for contracting. The definition included in H.R. 4015 is generally consistent with the definition contained in OMB Circular A-76. However, recently, some agencies' interpretations of inherently governmental functions in making contract awards have been questioned.

The degree of contractor involvement in the government's work is an important aspect of this issue. This bill specifies, for example, that the management and direction of the Armed Services is a governmental function which should not be contracted out. However, the question is to what degree is it proper for government officials who have the responsibility for managing the Armed Services to rely on the assistance of contractors. Is it sufficient to have a government official making the final decisions if most of the advice and analysis leading to those decisions is from contractors? We believe the question of where to draw the line between contractors and government officials is closely related to defining what is inherently governmental.

We are currently doing work for Senator Pryor to assess the extent to which government agencies might be contracting out functions which should be performed by government officials. Part of our work involves examining the adequacy of the current definition of inherently governmental functions to determine whether it is sufficiently clear, consistent, and precise. We will keep the Committee informed on our progress.

Seventh, the bill extends coverage to the U.S. Postal Service. The Postal Reorganization Act, enacted in 1970, permits the Postal Service to contract under its own rules and regulations, which differ from the uniform rules that apply to most other federal entities. The intent of the Postal Reorganization Act was to permit the Postal Service to operate more like a private business when it is advantageous to do so. Because Congress has deliberately excluded the Postal Service from federal procurement statutes and because of potential conflicts with its collective bargaining obligations, we believe that the Postal Service should not be subject to the provisions of H.R. 4015.

Eighth, the process set up by H.R. 4015 to resolve disputes

concerning contracting out decisions seems conceptually fair and equitable, thus we support agencies assuming that responsibility. However, we do think that section 12 of the bill, which amends 31 U.S.C., Section 3551(2) by providing that GAO's bid protest procedures are not applicable "to conversions to contract or conversions to in-house performance," should be clarified.

Protest issues that arise out of the competition among the commercial sources do not directly concern either the conversion cost analyses or the performance work statement. Protest issues involve claimed violations of the procurement laws and regulations, including such subjects as late bids, responsiveness, and responsibility. Since the dispute resolution process set up under H.R. 4015 deals solely with conversion cost analyses and performance work statement issues, we believe that it would be appropriate for GAO to continue to resolve protests arising out of the competition among commercial resources. In order to achieve this goal, we are providing suggested language to amend H.R. 4015 (See Appendix I).

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That concludes my prepared statement, Mr. Chairman. My colleagues and I would be pleased to respond to questions.

APPENDIX I

Achieving Cost Efficiencies in Commercial Activities

(GAO/G-GGD-90-35)

We suggest that section 12 of H.R. 4015 be amended to state:

Section 3551(2) of title 31, United States Code, is amended by striking "and" at the end and inserting in lieu thereof the following:

"except that in the case of protests concerning the cost comparison analysis or the performance work statement relating to a conversion to contract or a conversion to in-house performance by an agency under the Commercial Activities Contracting Procedures Act of 1990, such term does not include--

"(A) a commercial source; or

"(B) an employee of an agency; and"

The Committee Report would thus state:

This section would amend 31 U.S.C., Section 3551(2) by providing that GAO bid protest procedures are not applicable to protests concerning the cost comparison analysis or the performance work statement relating to conversions to contract out or conversions to in-house performance.